No. 14,450

United States Court of Appeals

For the Ninth Circuit

GEORGE W. LEWIS,
Appellant,

vs.

UNITED STATES OF AMERICA,
Appellee.

BRIEF FOR APPELLANT.

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STATEMENT OF JURISDICTION.

Appellant was found guilty by jury verdicts after trial in the United States District Court for the Northern District of California, Southern Division, of three violations of Section 145b of Title 26 U.S.C.A. Appellant was sentenced to a term of one year imprisonment on each count, the sentences to run concurrently and to pay a fine of $8,000.00 on each count. (T.R. 18-19.) Notice of appeal was timely filed. (Rule 37 (a) Federal Rules of Criminal Procedure.)

The jurisdiction of this Court to review the final judgment of the District Court is sustained by 28 U.S.C. Sections 1291, 1294.

STATEMENT OF THE CASE.

Appellant was indicted in the United States District Court for the Northern District of California, Southern Division. The indictment was in three counts. (T.R. 3-6.)

Each count charged a violation of Section 145 (b) of Title 26 U.S.C.A. The first count charged that the defendant on January 15, 1948, did wilfully and knowingly attempt to defeat and evade income taxes owing to the United States for the year 1947 by filing a false and fraudulent income tax return. This count alleged that he understated his income in the amount of $187,817.22 and that he asserted only $2,018.10 in taxes was due when the amount due and owing was $145,761.90.

The second count alleged a charge of wilful evasion in the same year as the first count by the filing of a false return on behalf of the defendant's wife. In connection with her return it is alleged that the understatement of income was $185,757.38. The tax due was $146,189.40, and the return showed only $2,884.55 in taxes due and owing.

The third count alleges a violation of the same statute involving income and taxes for the year 1948. It alleges a wilful attempt to defeat and evade taxes by the filing of a false and fraudulent joint return of the defendant and his wife; that the return set forth an income of $115,153.06 and a tax due of $53,113.62 while the true income was $308,099.51 and that the tax thereon was $199,834.82.

Motions to dismiss the indictment and for a bill of particulars were filed, argued and denied. (T.R. 7-16.) Thereafter the defendant entered his plea of not guilty to each count of the indictment (T.R. 16, and the case was tried before a jury. At the conclusion of the government's case the appellant made a motion to strike all of the testimony and evidence relating to the net worth and expenditure computations advanced by the government. (T.R. 559.) Likewise, pursuant to Rule 20(a) of the Federal Rules of Criminal Procedure a motion for a judgment of acquittal was made. (T.R. 559.) Both these motions were denied. (T.R. 559.)

The defendant introduced evidence on his behalf and testified. Rebuttal testimony was offered by the government. At the conclusion of all the evidence in the case another motion for judgment of acquittal was made and denied. (See Stipulation re Minute Order May 12, 1954, on file herein.)

The jury returned a verdict of guilty on each count. (T.R. 16.) The motion for judgment of acquittal was renewed and in the alternative a motion for a new trial was made. Both motions were denied. (T.R. 17.) The defendant was sentenced to one year imprisonment and a fine of $8,000 on each count. The terms of imprisonment were ordered to run concurrently. (T.R. 18-19.) A timely notice of appeal was filed. (T.R. 20.)

The transcript of record consists of approximately 950 pages. The theory upon which the government

based its case was the so-called "net worth and expenditures" method. It contended that expenditures in excess of reported income for the two years in question constituted the measure of unreported income for those years. The defendant contended that all of his income and that of his wife for the two years in question was properly reported and that expenditures in excess of reported income came from accumulations in prior tax years.

The evidence discloses that the defendant, who will be 65 years of age this year was born and raised in San Francisco. Starting with the year 1904 he began an association with horse racing, that continued in various capacities until the year 1948. (T.R. 613-651.) For many of his adult years he engaged in the business of "book-making" at various race tracks throughout the United States and in Canada and Mexico. For the two years mentioned in the indictment and for some years prior thereto he had been an official of the Detroit Racing Association acting in various capacities and for the year 1948 was general manager and president.

The government proceeded to attempt to prove a case of wilful evasion by showing a series of expenditures by the defendant in excess of his reported income for the two years in question. Its attempt involved the testimony of 35 witnesses and a series of stipulations both oral and written, dealing with the amount of money expended by the defendant in the two years in question.

As is customary the prosecution offered in evidence the original tax returns of the defendant and his wife for the year 1947 and their joint return for the year 1948. (Exs. 4-5-6, T.R. 30.) Immediately the prosecution thereupon placed in evidence, without foundation, and over the defendant's objection, a document purporting to show that the defendant was liable for taxes for the year 1933 arising from a liability transferred from another separate taxable entity. (Ex. 10, T.R. 34.) The government then offered a series of documents and testimony of two government officials, all over the objection of the defendant, relating to an effort to compromise such tax liability, terminating with an offer in compromise which was finally accepted in 1941. (T.R. 72, Ex. 14F.)

The offer so accepted was in the sum of $1,500.00 in settlement of a transferee liability of approximately $4,000.00. The deficiency was for unpaid excess profit taxes of an insolvent corporation of which the defendant had been an officer.

The government produced a series of witnesses, altogether 35, who testified as to various financial transactions they had with the defendant, or that they recorded as accountants for enterprises in which the defendant invested or identified other records. In addition numerous stipulations both oral and written were introduced into evidence concerning the fiscal affairs of the defendant. This testimony covered the years 1941 to 1948 and was introduced into evidence over the objection of the defendant.

The gist of the government's case was that for the two years in question the defendant had spent more than he had reported as income. Exs. 61, 62 and 63 (T.R. 467 and 494) were admitted in evidence, over the objection of the defendant, such exhibits comprising a summary by the government agents of funds available and funds spent for the period 1942-1948, by the defendant. For the convenience of the Court such exhibits are reproduced as an appendix to this brief and bear the same exhibit number as marked by the trial Court.

In short the prosecution's case consisted of showing that money was spent in excess of reported income over a seven year period, amounting to $832,993.06. (Appendix Ex. 62.) The government did not attempt to show either for the year 1947 or the year 1948, the two years with which the defendant was charged with wilful evasion of taxes, any of the following:

(1) That the records from which his tax returns were prepared were inadequate for that purpose;

(2) What the net worth of the defendant was at the beginning of both those years; or

(3) That the defendant had a source of income for those years other than that reported.

The government's chief witness who prepared the exhibits attached hereto and made the investigation in this case was Special Agent Klass of the Internal Revenue Service. (T.R. 456.) He explained the theory under which this prosecution proceeded, as follows (T.R. 464-465):

"Well I attempted to reconstruct his income for each of those years telling his actual income by the net worth method or an outgrowth of the net worth method called the source and application of funds method."

The government produced as its witness one William Anater who testified that he had prepared the three income tax returns that were the subject matter of this indictment. (T.R. 227-229.) On cross-examination he testified that he had records furnished to him by the defendant or others on the defendant's behalf from which he obtained the information which he inserted in the returns. (T.R. 298-299.) For the year 1948 an item of $43,198.44 being the so-called book profit of a partnership was not included in the appellant's return for that year. This witness on direct examination explained that he was the one that determined that the items should not be shown in that return. (T.R. 238-242.) Records which were introduced into evidence consisted of books of account of the various enterprises regularly maintained by accountants. The partnership transaction was fully disclosed on the books of account of this partnership and the witness testified that for technical accounting reasons the items should not be shown on the return of the defendant.

Only two witnesses testified as to a possible source of income to the defendant other than that reported. Earl Beasley, a government witness, testified that in the year 1947 or 1948, he was not sure which, the defendant had told him that he the defendant had

lost $125,000.00 betting on a horse owned by the witness. (T.R. 370.) It might not be inappropriate to point out that the government stipulated during the course of the trial that during 1947 and 1948 the defendant had loaned this witness $104,000.00. (T.R. 383, Ex. 57, Appendix Ex. 62.) The defendant sued to recover the loan in the United States District Court in Nebraska. (T.R. 384.) The deposition of this witness was taken prior to that trial and he stated that he had not gone to any safe deposit box with the defendant nor did he make mention of a $125,000.00 bet. After the appellant herein had testified at that trial the witness for the first time related the bet of $125,000.00. (T.R. 402-408.)

The other witness from whom the government sought to obtain testimony concerning a possible source of income was William C. Gaskill. He testified that in 1947 or 1948, he couldn't remember which, (T.R. 358) he heard the defendant request another party present to make a bet on a horse in the amount of $15,000.00; that he did not know if the bet was made; that he did not see the defendant give any money to the other party (T.R. 359); but that two or three hours later he saw the defendant give such party a paper bag. (T.R. 360.)

The defendant took the stand on his own behalf. He testified as to his various activities in the racing world covering almost 50 years. He testified that as a result of bookmaking activities throughout the United States he had acquired $1,000,000.00 in currency by the year 1930, (T.R. 631), and that this

money was kept in several different suitcases. Several witnesses corroborated the defendant's testimony in this respect. Each of them testified to his having large sums of currency prior to 1941, the so-called starting point of the government's net worth calculations.

The first was the government's witness John T. Laird. He had been examined extensively by the government with relation to numerous financial transactions he had with the defendant commencing with the year 1942 through 1948. (T.R. 408-425.) Upon cross-examination it was sought to elicit information concerning a financial transaction in 1941. (T.R. 427-428.) The government's objection on the ground that such questions were beyond the scope of the direct examination was sustained. (T.R. 428.) The Court required the defendant to make the witness a defense witness after an offer of proof. (T.R. 430-432.)

The witness testified that in the year 1940 or 1941 the appellant offered him $100,000.00 in currency to negotiate the purchase of the San Diego baseball club. (T.R. 435.) The defendant's wife testified that in the year 1928 the defendant was possessed of currency which he kept in a suitcase. (T.R. 563.)

Likewise the witness Normile testified to the defendant's possession of large amounts of currency in the years 1927-1928-1929 and to his earnings as a bookmaker. (T.R. 581-605.) Also a deposition of a witness John Geddert was read (T.R. 580) concerning currency in the possession of the defendant at

times prior to 1941. The original deposition was transmitted to this Court as an exhibit.

The defendant likewise testified that in the early 1940's an agent of the Internal Revenue Bureau called upon him and that he offered to allow him to count the money in the suitcase. (T.R. 723.) The agent was not called as a rebuttal witness by the government.

SPECIFICATION OF ERRORS RELIED UPON.

1. Insufficiency of the evidence to establish the charges or to support the verdict and/or judgment of the charges contained in the indictment.

2. That the District Court and the judge thereof erred in denying appellant's motion for judgment of acquittal made at the conclusion of the plaintiff's case.

3. That the District Court and the judge thereof erred in denying appellant's motion for judgment of acquittal made at the conclusion of the presentation of all of the evidence in the case.

4. That the verdicts were contrary to the weight of the evidence.

5. That the verdicts and each of them were not supported by substantial evidence.

6. The Court erred in admitting in evidence on behalf of the government all of the Exhibits and testimony to which objection was made by the appellant and over the objection of appellant.

7. The Court erred in permitting the government to proceed to attempt to prove the allegations of the indictment by the application of the so-called "net worth" theory of proof.

ARGUMENT.

1. SUMMARY OF ARGUMENT.

There is no competent evidence from which a jury could conclude that there was a wilful attempt to defeat or evade income taxes for the two years in question. The only basis on which the verdicts could be explained, but not sustained, was that the defendant spent more money than he reported and therefore he was guilty.

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2. THE GOVERNMENT FAILED TO PRODUCE EVIDENCE OF A WILFUL ATTEMPT TO EVADE INCOME TAXES FOR THE TWO YEARS NAMED IN THE INDICTMENT.

Specifications of error Nos. 1 to 7.

All of the specifications of error may be considered under this one heading because they all expose the fatal flaw in the government's case. There was no evidence of a wilful attempt to defeat or evade income taxes as charged in this indictment. Faced with this fact the prosecution proceeded on its version of a so-called "net worth" method of proof. This method of proof did not attempt to follow the somewhat nebulous criteria established by the Courts heretofore concerning the net worth cases which criteria

are presently under the scrutiny of the Supreme Court.

See the following:

Goldbaum v. United States, 204 F. (2d) 74 (Cir. 9) Cert. denied October 12, 1953, 74 S.Ct. 39, 346 U.S. 831. Rehearing denied November 9, 1953. Order for cert. vacated June 7, 1954, 74 S.Ct. 861;

McFee v. United States, 206 F. (2d) 872 (Cir. 9). Cert. denied March 15, 1954, 74 S.Ct. 528, 347 U.S. 927. Order denying cert. vacated June 7, 1954, 74 S.Ct. 862;

Holland v. United States, 209 F. (2d) 516 (Cir. 10) Cert. granted June 7, 1954, 74 S.Ct. 863;

Smith v. United States, 210 F. (2d) 496 (Cir. 1) Cert. granted June 7, 1954, 74 S.Ct. 868;

Friedberg v. United States, 207 F. (2d) 777 (Cir. 6) Cert. denied, 74 S.Ct. 514; 347 U.S. 916. Cert. granted June 7, 1954, 74 S.Ct. 862.

The scheme employed by the prosecution is best described in the words of its chief witness Agent Klass:

> "Well I attempted to reconstruct his income for each of those years telling his actual income by the net worth method or an outgrowth of the net worth method called the source and application of funds method." (T.R. 464-465.)

Whatever sanction has been given the "net worth" method of proof by the Appellate Courts has not as

yet, in any reported case, been extended to this so-called "outgrowth".

This Court is too familiar with the principles of law governing the so-called "net worth" method of proof, to require an extended discussion. It may be said at the outset that this method of proof requires three elements to be proven beyond a reasonable doubt.

(a) A clear, concise and reasonably accurate determination of the net worth of the taxpayer at the start of the taxable period.

Calderon v. United States, 207 F. (2d) 377 (Cir. 9).

(b) A source of income during the period—that is for each of the years in question.

Schuerman v. United States, 174 F. (2d) 397 (Cir. 8).

(c) A net worth of the taxpayer at the end of the tax period that exceeded the sum of his net worth at the beginning of the period, his reported income and established personal expenditures during the period.

Bryan v. United States, 175 F. (2d) 223 (Cir. 5);

United States v. Fenwick, 177 F. (2d) 488 (Cir. 7).

In this prosecution not one of these principles was adhered to. Without establishing the fact or prima facie proof thereof, that the true income of the defendant could not be established from adequate

records for the two years in question, the government introduced into evidence, over his objection, extra judicial statements of the defendant concerning his financial position in the year 1941. These consisted of various offers in compromise made in that year and ultimately accepted in that year, the last being dated October 8, 1941. (Ex. 14F, T.R. 72.) Also included was a financial statement dated in November of 1941. (Ex. 58, T.R. 342-344.) The defendant testified that both these statements were untrue and were made with the advice of counsel for the purpose of avoiding the payment of disputed and contested claims for additional taxes. (T.R. 655-667.)

The government proceeded thereupon to introduce evidence over the objection of the defendant as to the expenditures of the defendant for the period 1942 to 1948. The extent of the government's proof is summarized by Exhibit 62 set forth in the Appendix hereto. It shows that for that period the defendant expended, according to their calculations $832,993.06 in execess of the amount of funds available. Notwithstanding that the charge was wilful evasion of taxes for the years 1947-1948 all of the testimony as to prior years expenditures was received in evidence without any attempt on the part of the government to prove that the returns for the two years in question were false.

The government's own witness William Anater testified that he had records furnished to him by the defendant or others on his behalf from which he obtained the information and entries inserted in

the returns. (T.R. 298-299.) The accuracy of these records was not assailed by the government.

(1) Beginning net worth not established.

At the outset of this argument we stated that this case did not proceed upon a "net worth" theory but upon the so-called "out-growth" characterized as the "source and application of funds method". The government did not fix with certainty or at all the net worth of the defendant at the beginning of either of the tax years. Without such a foundation the proof of excess expenditures is not sufficient to prove income and evasion of tax thereon beyond a reasonable doubt. As was stated in the case of *United States v. Fenwick,* (Cir. 7) 177 F. (2d) 488 (1949):

> ". . . when the government relies upon circumstances of increased net worth and expenditures in excess of reported income to establish income tax evasion, the basic net worth must be established."

Here the basic net worth was the net worth for the first year mentioned in the indictment, 1947. That was the first charge of income tax evasion. The record is silent as to any proof as to the net worth of the defendant as of January 1, 1947. Likewise, as to his net worth for the other year in which he is charged with income tax evasion, 1948.

That this basic premise was not established is demonstrated by the government's Ex. 62 (Appendix) which shows according to the government's computations that the defendant's expenditures in the year

1946 exceeded funds available to spend by the sum of $159,633.93. On the same exhibit is recorded three loans made by the defendant within the first 16 days of January, 1947, in the total amount of $115,000.00, being the loans to Harold Ephlin (item 26) William Lias (item 42) and the North Bay Builders (item 43). That these transactions occurred within that period and were in cash was stipulated to by the government. (T.R. 876-877.)

The government offered no proof as to the source of these funds nor did it attempt by competent proof to exclude the hypothesis that such funds were available from accumulation in previous non indictment years.

In the *Fenwick* case (supra) the Court stated:

> "Of course, before the increased net worth method of proof is effective, the net worth of the taxpayer at the beginning of the tax year must be clearly and accurately established by competent evidence. (Citing cases). By this rule we must test the sufficiency of the evidence offered by the government to establish defendant's net worth at the beginning of 1943".

By the same rule we must test the sufficiency of the evidence offered by the government to establish defendant's net worth at the beginning of 1947. It is submitted that that evidence is totally lacking. Realizing that such was the case the prosecution attempted to rely upon the so-called "outgrowth" of the net worth theory and move the starting point back to a non-indictment year based on extrajudicial

admission of the defendant, without more. They then lumped together 7 years of receipts and expenditures, and the latter being greater than the former, secured his conviction of income tax evasion during the last two years.

The defendant was on trial only on the charges contained in the indictment, to-wit: that he wilfully attempted to defeat and evade income taxes for the years 1947 and 1948 by filing false and fraudulent income tax returns. Under that indictment he could not be tried for evasions in any years previous. By this method of proof he was required to defend against the unwritten accusation that he had defaulted in his tax obligations for each year commencing in 1942. This the law requires of no defendant notwithstanding the adroitness of prosecuting attorneys or revenue agents in contriving "outgrowths" of means of proof that violate every principle of criminal justice.

United States v. Fenwick, (7th Cir.) 177 F. (2d) 488 (1949):

"Remembering that the government has the burden of proof in a criminal case, that the burden never shifts to defendant, that circumstantial evidence must be of such character as to exclude every reasonable hypothesis except that of guilt, it necessarily follows that, when the government relies upon circumstances of increased net worth and expenditures in excess of reported income to establish income tax evasion, the basic net worth must be established. The defendant is not compelled to take the witness

stand; he is not compelled to make proof that he is innocent, but he must be proved guilty by the evidence beyond all reasonable doubt, and where there is uncertainty as to whether all the assets of defendant are included in the government's computation of net worth, it follows that its computations can not be relied on. Essential proof of no other assets is the cornerstone of the evidence of the government; that cornerstone being faulty, the whole edifice is so weakened as to be undependable as proof of guilt beyond all reasonable doubt."

(2) No source of income proved for the indictment years.

As indicated before only two witnesses testified with reference to a possible source of unreported income to the defendant. To so characterize the gist of their testimony is to view it in a light more favorable to the government than the testimony warrants. An examination of their testimony compels the conclusion that at most it permitted the jury to speculate and surmise that there might be a possible source of funds. This a jury is not permitted to do.

The government offered no direct testimony of unreported income items or of any undisclosed source of income. Faced with this lack of proof of an essential ingredient to a charge of wilful evasion they produced two debtors of the defendant. The first was Earl Beasley. The government at the outset of the trial stipulated that he was indebted to the defendant in the sum of $104,000.00. (Stipulation 57; Appendix Ex. 62, item 41.) On cross-examination he

repudiated this stipulation and denied the debt. (T.R. 391.)

This witness on direct examination related a conversation with the defendant wherein he claimed that the defendant had informed him that he had lost $125,000.00 betting on a horse owned by the witness. (T.R. 369-371.) He could not recall whether the conversation occurred in 1947 or 1948. He could not recall where or when the race was run. It was established without contradiction that the only time this particular horse raced with the particular jockey was on December 3, 1948. (Defs. Ex. L, T.R. 703.)

The second such witness was William Gaskill. He testified that he was present in the defendant's home and heard a conversation with reference to a $15,000.00 wager. (T.R. 358-359.) He could not remember whether it was 1947 or 1948. He did not see any money change hands, nor did he know if the bet was made.

Even giving full credibility to this testimony it does not establish a source of unreported income nor does it tend to prove with any reasonable certainty the year in which the occurrence took place.

There was no proof direct or circumstantial that the defendant was engaged in any business, during the indictment years, legal or illegal, other than those disclosed on his income tax returns. There was no proof of concealment or destruction of records. There was no evidence, and there could be none of illicit or unlawful activities or a background thereof.

The Supreme Court in the case of *United States v. Johnson* (1943), 319 U.S. 503, stated that it was necessary to find that the defendant was engaged in an income producing business legal or illegal. In that case involving a gambling house operator and owner the Supreme Court reviewed the evidence submitted by the government showing that there had been gambling transactions on an enormous scale that were overwhelmingly established by the government's proof and pointed out that the long duration of the gambling business, the substantial evidence of the law of probability in favor of the gambling houses, records pertaining thereto, all supported the government's contention that the defendant during the indictment years enjoyed a source of income therefrom. After reviewing all of these factors the Court stated that this evidence:

> "made it not a *matter of tenuous speculation but of solid proof* that there were winnings of a substantial amount which Johnson did not report." (Italics supplied.)

Comparing the proof in that case with the instant record shows that based on the testimony of these two witnesses the jury was permitted to engage in the tenuous speculation that this defendant for the years included in this indictment had unreported income from any source.

Here in this case all the government attempted to do was prove a series of expenditures both in the indictment years and in years previous thereto. It made no attempt to fix the net worth of the defendant

at the beginning of the tax years in question, and thus establish that such expenditures as were made in those years did not come from previous accumulations, and it made no attempt to prove the possible source of those expenditures during the two years in question. Having thus concluded its case, it placed the burden upon the defendant of proving his innocence. As this Court knows, it is sometimes impossible for a defendant to prove his innocence and the law wisely does not require that of him. By proceeding on a sheer expenditure method of proof over the period in question here, the defendant was called upon not only to answer the charges contained in the indictment but to explain variances between income and outgo over a period not included in such indictment.

This method of proceeding was commented upon by Meyer Rothwacks in a paper entitled "Indirect Proof of Income in Tax Evasion Prosecutions" submitted at the Symposium of the American Bar Association, Section of Taxation, on Tax Fraud Proceedings and Law, September 1950, Washington, D.C. There the author stated:

> "Permitting a case to go to the jury predicated upon expenditures plus a possible source of income, means that the jury may bring in a verdict of guilty although the government has not proved a case beyond a reasonable doubt. Indeed, a verdict of guilty rests upon the probability that a defendant who fails to explain satisfactorily the source of his expenditure had received unreported income during the tax year. Thus, the

> prosecution is permitted to prevail, not by adducing evidence inconsistent with innocence, but by shifting the burden of adducing evidence to the defendant. No longer may a defendant sit back and wait for the government to prove his guilt. And even if a defendant attempts to explain the source of his funds, the jury need not accept that explanation."

See Balter, "Fraud Under Federal Tax Law", page 291, Footnote 28.

(3) Failure to prove a net worth at the end of either of the tax periods.

As stated above this case proceeded on the theory that every dollar spent by the taxpayer in excess of his reported income in any given year, was taxable unreported income for that particular year. This theory is not supported by the evidence or the authorities. It is a false theory unless it is shown with what assets or resources the taxpayer was possessed at the beginning of the indictment year, what his sources of income were during the year, and finally his net worth at the end of the year. These are the circumstantial measuring sticks and without any or all of them there is no true measure.

The government offered no proof of the defendant's net worth at the close of 1946, whereby his income for 1947 could be measured. Because no closing net worth for the year 1947 was proven no measure of income was available for 1948. Without these the whole case of the government depended upon a showing of expenditures by the defendant in excess of

reported income, without excluding the reasonable hypothesis that such excess expenditures were possible through previous accumulations in non-indictment years.

The case of *Bryan v. United States,* 175 F. (2d) 223 (Cir. 5) is one which is familiar to this Court. There the government sought to prove a case of wilful evasion of income taxes for a four year period. There was no direct testimony of failing to account for gross income, false deductions or false books and records. The government showed by the testimony of approximately fifty witnesses and by documentary proof that the defendant had made expenditures in each of the indictment years of sums greatly in excess of the gross income reported for each year.

The government insisted that the defendant's net worth during each year in question was increased by expenditures made in excess of reported gross income. The defense, as here, was that the evidence failed to show that the expenditures in excess of reported gross income came out of current receipts and not out of available assets acquired by him in prior non-indictment years.

The defense there, as here, was that the defendant had amassed considerable wealth in years prior to the indictment years and secreted the same in the form of currency in defendant's home.

In reversing the conviction the Court stated:

> "The net worth expenditures method of establishing net income, sought to be applied in this case, is effective only if the computations of net

worth at the beginning and at the end of the questioned periods can reasonably be accepted as accurate."

The Court pointed out in that case that the evidence failed to show a lack of additional assets at the beginning of the tax period, and for that reason should not have been submitted to the jury. Here the evidence failed to show a lack of additional assets at either the beginning of the tax period January 1, 1947, or the end of the tax period December 31, 1947, covered by the first two counts of the indictment or at the beginning and close of 1948.

We submit that here as in the *Bryan* case the evidence was circumstantial and failed to exclude every reasonable hypothesis other than the guilt of the defendant.

CONCLUSION.

In no reported case has the government attempted to convict a defendant of a wilful attempt to defeat or evade income taxes on the theory advanced here. Without establishing the inadequacy of records maintained on behalf of the defendant reflecting his income for the two years contained in the indictment and without establishing by any recognized form of competent evidence a source of income in addition to that reported for these years, the government was permitted to proceed on what it terms an "out

growth" of the net worth method of proof to secure the conviction of the defendant of spending too much money.

Had this been a proper case for the application of any judicially recognized method of proof still the government would have failed. It failed to establish the keystone of such a case, the starting point net worth of the defendant at the beginning of 1947, the first year of the indictment.

The defendant by his plea of not guilty put in issue the charges contained in this indictment. He was not called upon to plead to any charge not contained therein. The government did not proceed to prove the charges contained in the indictment but placed in evidence a series of expenditures for seven years that exceeded his reported income. It failed to exclude the reasonable hypothesis that for the years 1947 and 1948 the excess of expenditures did not come from previous accumulations in prior non-indictment years.

The government notwithstanding its failure to prove the charges contained in the indictment by adducing evidence pertaining to the years involved inconsistent with the defendant's innocence, shifted the burden of proof to the defendant. It not only shifted to the defendant the burden of proving his innocence to the charges contained in the indictment but to the unwritten charges which were the true "outgrowth" of the method employed by the government and permitted by the trial Court.

For the reasons herein set forth it is submitted that the evidence is insufficient to support these convictions and the same should be reversed.

Dated, San Francisco, California,
November 5, 1954.

Respectfully submitted,
JAMES E. BURNS,
Attorney for Appellant.

(Appendix Follows.)